

In the Matter of the Appeal of)
) No. 84A-724
GARY SALENGER)

For Respondent: Mary Olden
Counsel

This appeal is made pursuant to section 18593^{1/} of the Revenue and Taxation Code from the action of the Franchise Tax Board on the protest of Gary Salenger against a proposed assessment of additional personal income tax in the amount of \$1,950 for the year 1980.

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The sole issue to be decided in this appeal is whether or not the loss claimed on appellant's tax return for the year at issue is a business or nonbusiness bad debt.

During the year at issue, appellant, a dentist, was engaged in the full-time practice of dentistry. He also was employed as a part-time teacher at the University of California at Los Angeles. In 1978, appellant and Dr. Robert J. Verruso organized S.C.T.A., a corporation, of which they were the sole officers and shareholders. S.C.T.A.'s only business was a bar, Bill Bailey's. Dr. Verruso worked full time at the bar and appellant reduced his part-time teaching hours to devote time to Bill Bailey's. Appellant never received a salary or other remuneration for the time spent working at the bar. Both shareholders loaned money to the corporation. The business was not a success and, at appellant's insistence, it was sold. On his 1980 personal income tax return, appellant deducted \$2,500 (the amount of stock appellant purchased in the corporation) as a loss on small business corporation stock. Appellant also sought to deduct \$18,750 (the unrepaid portion of his loan to the corporation) as a debt incurred in his trade or business. Respondent disallowed the \$18,750 deduction, to the extent it exceeded the \$1,000 capital loss limitation, on the grounds that the loan was a nonbusiness bad debt rather than a business bad debt. This timely appeal followed.

Respondent contends that the trade or business of a corporation is not the trade or business of its shareholders and that appellant did not make the loan to protect his job and livelihood; therefore, the deductibility of appellant's loss is controlled by the nonbusiness bad debt provisions of the Personal Income Tax Law. Appellant argues that his dominant motivation in extending the loan was to secure a steady and profitable livelihood and, therefore, the bad debt clearly should be considered a business bad debt.

Where a business debt is proven to exist and it is totally worthless, the debt is treated as an ordinary loss and is totally deductible from income. (Rev. & Tax. Code, § 17207, subd. (a).) Where a nonbusiness bad debt is proven to exist and it is totally worthless, it is treated as a loss from the sale of a capital asset and is subject to the capital loss limitations of section 18152. (Rev. & Tax. Code, § 17207, subd. (d)(1).)

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A business bad debt deduction is one based on a debt created or acquired in connection with the trade or business of the taxpayer. It is now well established that being an employee may constitute a trade or business for the purposes of determining whether a debt is a business debt. (Trent v. Commissioner, 291 F.2d 669 (2d Cir. 1961); Putoma Corp. v. Commissioner, 66 T.C. 652, 673 (1976).) In determining whether a bad debt has a proximate connection with a trade or business of the taxpayer, we must determine the dominant motivation of the taxpayer. (United States v. Generes, 405 U.S. 93, 103 [31 L.Ed.2d 62] (1972).) The determination of a taxpayer's dominant motive is essentially a factual inquiry, with the burden of proof on petitioner. (Putoma Corp., supra; Smith v. Commissioner, 55 T.C. 260 (1970), remanded for consideration in light of Generes in 457 F.2d 797 (5th Cir. 1972), opn. on remand, 60 T.C. 316 (1973).)

In the Appeal of David B. Haag and Estate of Carol D. Haag, Deceased, decided by this board on December 13, 1983, we concluded that advances to a corporation owned by the taxpayer, a practicing dentist, and three other individuals were business debts. Although the taxpayer was a practicing dentist, he devoted 25 to 30 hours a week to the corporation which developed and marketed motorcycle parts. His testimony convinced this board that his dominant motivation in making the loans was, in fact, to protect his employment relationship with the new corporation rather than his investment interest and that he, in fact, had a wish to establish a new career. In the Appeal of James C. and Antoinette Glaser, decided by this board on September 28, 1977, we concluded that future employment as opposed to the financial incentive of equity ownership was not the dominant motivation for a taxpayer employed at a bottling plant who began a vending machine operation in which he worked nights and weekends.

In the instant case, appellant maintained a full-time dentistry practice and his part-time teaching job during the time he was a part owner of Bill Bailey's. Although he did reduce his teaching hours to spend more time at the bar, there is no indication, in contrast to the taxpayer in Haag, supra, that he was planning to abandon his dentistry practice for a new career as a bar owner or bartender. As such, we must conclude that unlike Mr. Haag, appellant's dominant motivation in making the loan was not, in fact, to protect an employment relationship with the corporation, but rather, like the taxpayer in Glaser, supra, his motivation was the

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financial incentive of equity ownership in an investment. Appellant has not presented any evidence which would lead us to a different conclusion.

For the reasons stated above, we conclude that respondent's action in this matter must be sustained.

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O R D E R

Pursuant to the views expressed in the opinion of the board on file in this proceeding, and good cause appearing therefor,

IT IS HEREBY ORDERED, ADJUDGED AND DECREED, pursuant to section 18595 of the Revenue and Taxation Code, that the action of the Franchise Tax Board on the protest of Gary Salenger against a proposed assessment of additional personal income tax in the amount of \$1,950 for the year 1980, be and the same is hereby sustained.

Done at Sacramento, California, this 9th day of October, 1985, by the State Board of Equalization, with Board Members Mr. Dronenburg, Mr. Collis, Mr. Bennett, Mr. Nevins and Mr. Harvey present.

<u>Ernest J. Dronenburg, Jr.</u>	, Chairman
<u>Conway H. Collis</u>	, Member
<u>William M. Bennett</u>	, Member
<u>Richard Nevins</u>	, Member
<u>Walter Harvey*</u>	, Member

*For Kenneth Cory, per Government Code section 7.9